STANDARD & POOR'S **Global Credit Portal®** RatingsDirect

Research

Summary:

Hawaii
Hawaii Harbor Division; Ports/Port Authorities

01-Dec-2011

Current Ratings

Credit Profile

Hawaii		
Hawaii Harbor Div, Hawaii		
Hawaii (Hawaii Harbor Division)		
Long Term Rating	A+/Stable	Outlook Revised
[+] **Hawaii (Hawaii Harbor Div)**		
Unenhanced Rating	A+(SPUR)/Stable	Outlook Revised

Many issues are enhanced by bond insurance.

Rationale

Standard & Poor's Ratings Services revised the rating outlook to stable from negative on **Hawaii**'s $379.8 million in bonds outstanding, issued for **Hawaii Harbor Division**. At the same time, Standard & Poor's affirmed its 'A+' long-term and underlying rating (SPUR) the bonds.

The outlook revision reflects our assessment of the division's improved operational measures and financial margins. The ratings are based on our view of the port system's dominant business position and importance to the state's economy, as well as recent tariff increases designed to address volume declines and eroding financial metrics and to support the capital improvement program.

More specifically, the rating actions reflect our view of:

- The system's monopolistic position as Hawaii's sole provider of maritime facilities and services;
- The importance of the system to the state, as approximately 80% of the total volume of goods consumed in Hawaii are imported and roughly 98% are processed through the system;
- The system's strong liquidity, with 773 unrestricted days' cash on hand (DCOH) in fiscal 2010; and
- Annual planned tariff increases effective beginning March 1, 2010 that resulted in a 17% growth in fiscal 2011 operating revenues (outperforming the 12% expected), as well as a schedule of annual tariff increases in 2011 through 2015.

The preceding credit strengths are offset in part by our view of:

- An annual average decline of 6.2% in cargo tonnage for 2007 to 2010, with a corresponding drop in port revenues averaging 5.4% a year (however, fiscal 2011 cargo tonnage rebounded, increasing by 1.3%), and

- The system's significant capital needs totaling about $600 million through fiscal 2015 to address the large port system's expansion and maintenance requirements. Management has stated that the capital plan is prioritized and that projects will be undertaken only once funding becomes available.

A senior lien on the system's net revenues secures the bonds. In addition to the revenue-secured bonds, the division is obligated to pay from revenues on a subordinated basis annual debt service associated with approximately $36 million in reimbursable state general obligation bonds outstanding it used to construct facilities for an interisland high-speed ferry (Hawaii Superferry Inc.) that has since filed for bankruptcy. All revenue-secured debt outstanding is fixed rate and matures July 1, 2040.

Similar to many ports and port systems, Hawaii's harbor system experienced large declines in operating performance measures (tonnage, ship calls, and cruise passengers, for instance) due to the recent recession, resulting in lower revenues and eroded financial metrics. We view the division's monopoly position and essential role as a fundamental credit strength. We also view management's recent actions to adjust tariffs to compensate for volume declines and finance needed capital improvements as a positive credit factor. As a whole, Hawaii imports 80% of its required goods, with 98% shipped via water. The division oversees a system of 10 harbors on six islands throughout the state and is a landlord port operator with terminal operators directly hiring stevedoring firms. Unlike other large landlord container ports, the division is more exposed to revenue swings associated with volume fluctuations. The wharfage component of total operating revenues is high, in our view, at 52% in fiscal 2010 compared to rentals at 33%. The two harbor facilities supporting the most populous island of Oahu were responsible for 81% of operating revenues in fiscal 2010. Honolulu Harbor, the system's largest, accounts for nearly 50% of system tonnage. It operates as the transshipment hub for cargo shipped from the U.S. mainland to all islands through Oahu. It has a main harbor basin with a depth of 40 feet, more than 30 berths, five linear miles of mooring space, and 230 acres of cargo handling area. Some facilities are owned by the federal government and private companies, and the state owns the majority of the land although both the U.S. Coast Guard and Chevron Corp. have significant holdings.

Cargo volume tonnage has fluctuated somewhat during the past five years. Honolulu experienced declines in fiscal 2008 (1.0%), fiscal 2009 (11.4%), and fiscal 2010 (0.4%), compared with overall system decreases of 2.0%, 13.1% and 3.5%, respectively. However, volumes rebounded in fiscal 2011, increasing by 0.8% for Honolulu and by 1.3% for the system overall.

Total operating revenues declined to $73.3 million in fiscal 2010 (similar to fiscal 2003 results) from a peak of $85.6 million in fiscal 2007. However, as a result of the tariff increases effective March 1, 2010, total operating revenue grew by 17.2% to $86.0 million in unaudited fiscal 2011, greater than fiscal 2007. Given the schedule of tariff increases through fiscal 2015, management projects total operating revenue will grow 8.9% in fiscal 2012, 7.7% in fiscal 2013, 7.4% in fiscal 2014, and 5.4% in fiscal 2015. In addition to the scheduled tariff increases through 2015, a mechanism was created to increase the cargo tariffs annually by 3% or Consumer Price Index from 2016 onward.

Debt service coverage (DSC) has dropped to 1.6x in fiscal 2010, which we consider adequate, from 2.2x in fiscal 2007, excluding eligible fund balances, and to 2.1x in fiscal 2010 from 2.6x in fiscal 2007 including them. Liquidity measures including just the unrestricted cash and investments increased to 773 DCOH in fiscal 2010, which we view as strong, although down from 2007's 1,065 DCOH. Management estimates unaudited fiscal 2011 DCOH will increase to 869.

We view the division's recent tariff rate increases (preceded by an increase in 1997) and schedule of proposed increases favorably; we also consider the system's ability to tap federal grant sources of capital funding reduces debt levels as a positive credit factor. The system projects increased revenues due to tariff adjustments and economic recovery as well as expense controls. Management's forecast shows DSC levels will decline to a low of 1.5x in 2013 on a cash flow basis and 1.9x calculated as per the rate covenant. Unaudited fiscal 2011 DSC is expected to be 2.0x on a cash flow basis and 2.4x including fund balance.

In our view, the division's capital plan is large and could pressure debt levels in the long term. The Harbors Modernization Plan originally totaled $618 million for 2010 through 2015 in harbor infrastructure improvements statewide. Approximately $600 million remains in the plan. Management has identified $164 million in priority projects from within this plan and indicates it will undertake other projects as funding becomes available. While the system's expansive and essential nature provides for a strong business position, it also requires significant investment in facilities that individually sometimes do not have the commercial activity to fully support capital and operational costs. Also, the division often participates in economic development projects (for instance, Hawaii Superferry) that can add to the overall debt burden without commensurate revenue growth.

In our view, the state's economy is beginning to recover following a slowdown in construction and tourism. However, island unemployment and housing sector declines were less severe than those of other states, and federal spending, particularly for defense projects, has stabilized.

Outlook

The stable outlook reflects our opinion of the improved financial margins and implementation of new tariffs and cost controls. We could take a negative rating action during the two-year outlook timeframe if the system incurs a significant amount of additional debt and financial margins deteriorate. We do not expect to raise the ratings during the next two years.

Related Criteria And Research

USPF Criteria: **Port Facilities Revenue Bonds**, June 13, 2007

Complete ratings information is available to subscribers of RatingsDirect on the Global Credit Portal at www.globalcreditportal.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.

Primary Credit Analyst: Mary Ellen Wriedt, San Francisco (1) (415) 371-5027; **maryellen_wriedt@standardandpoors.com**

Secondary Contact: Paul Dyson, San Francisco (1) 415-371-5079; **paul_dyson@standardandpoors.com**